Financial Markets

Irving Trust

Irving Trust Company
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Economic Research &
Planning Division

Friday
(Noon)

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Financial markets ran the gamut of emotions this week, from utter despair early in the week to emerging optimism later on. The $6.9 billion increase in the money stock reported last Friday plus the soaring Federal funds rate after the weekend were critical factors, as was the highly pessimistic interpretation given Chairman Volcker's testimony at the monetary policy oversight hearings this week. In that setting, not even the Wednesday GNP report--which pointed to considerably more economic sluggishness than had generally been realized--could help much.

Volcker's testimony was much more revealing than most newspaper accounts suggested. He confirmed that the FOMC had decided for the duration of the year to aim for the bottom of the 3 1/2%-6% target range for shift-adjusted M-1B as well as the top of the M-2 range. As usual, the M-1B range for next year was moved down slightly from this year's range. As was widely expected, no target will be set next year for M-1A, which has been rendered obsolete by the expansion of NOW accounts.

As noted here last week, the M-1B and M-2 targets were clearly inconsistent, so that something had to be done. Thus the implicit change in this year's targets was hardly the policy "tightening" reported in a number of press accounts--indeed, the Chairman went to some lengths to clarify its technical nature. Nor was next year's lower range for M-1B (soon to be known simply as M-1).

These actions do confirm that the Fed is pursuing a more restrictive policy than many had thought. That lessens the chance for sharp declines in rates by year-end, though it certainly does not rule out a gradual downward trend.

Naturally, much depends on the pace of economic activity in coming quarters. The FOMC expects very sluggish growth in real GNP to carry into 1982. The report noted pointedly that the Administration's more optimistic scenario "would seem to depend on a substantial rebound in productivity in the wake of tax and regulatory changes now in prospect, and, relative to historical experience, on a considerable willingness by the public to economize on cash balances in response to continuing changes in financial technology and other factors." Translation: The FOMC thinks its monetary targets are inconsistent with the pickup in real growth envisioned by the Administration.

Finally, Volcker emphasized the need to produce palpable improvement on the inflation front and/or economic slack in advance of labor negotiations beginning early next year, which he fears could set a pattern of excessive wage increases for some time to come. In the FOMC's view the next several quarters are thus especially crucial in the inflation fight.

In sum, it was a thoughtful report, well worth reading.

William C. Melton

Note: The full text of this letter is available to Telerate subscribers on pages 7250-51 on the Monday morning following the Friday date of the letter.

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Market Yields

	7/24/81 (Noon)	Week Ago	Year Ago
Prime Lending Rate at Irving Trust Company	20.50%	20.50%	11.00%
Effective since	7/8/81		
Discount Rate at Federal Reserve Bank	14.00	14.00	11.00
Federal Funds	18.50	17.75	8.63
Repurchase Agreements	17.63	17.25	8.50
U.S. Treasury Issues			
Bills			
3 months	15.97	14.85	8.25
6 months	16.38	15.36	8.44
1 year	16.04	15.59	8.60
Coupons			
2 years	15.61	14.95	9.03
4 years	15.12	14.59	9.42
7 years	14.64	14.24	10.15
10 years	14.40	14.03	10.20
Long Bond	13.65	13.35	10.24
Negotiable Certificates of Deposit-Secondary Market			
1 month	18.30	17.65	8.50
3 months	18.20	17.45	8.55
6 months	18.00	17.15	8.70
1 year	17.40	16.50	9.00
Banker's Acceptances			
1 month	18.60	17.50	8.50
3 months	18.40	17.60	8.50
6 months	18.30	17.40	8.45
Eurodollar Deposits			
1 month	18.88	18.44	8.88
2 months	18.75	18.38	8.94
3 months	18.88	18.44	9.06
Commercial Paper - Prime Names			
Directly placed by:			
Finance Companies			
1 week	18.25	17.38	7.00
1 month	17.50	17.00	8.38
3 months	16.75	16.75	8.38
Bank Holding Companies			
1 month	17.75	17.25	8.38
Dealer Placed:			
3 months	17.75	17.00	8.38
New AA Corporate Utility Bond	16.75	16.35	11.90
Tax Exempt			
6 month Project Notes	7.80	7.75	4.55
1 year AAA Bond	8.00	7.80	5.10
5 year AAA Bond	8.45	8.70	5.40
20 year AAA Bond	10.40	10.20	7.20

This information represents prevailing market yields.
It should not be construed as an offering.
All yields are on the offered side of the market.

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